

**MINUTES FROM THE INVESTMENT SUBCOMMITTEE
OF THE CASH MANAGEMENT POLICY BOARD**



Kenneth A. Simpler
State Treasurer

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Mr. John Flynn, Chair, Cash Management Policy Board
Mr. Dave Marvin, Chair, Investment Subcommittee
Mr. Mike Karia, Co-Chair, Investment Subcommittee
The Honorable Thomas J. Cook, Secretary, Department of Finance
The Honorable Ken Simpler, State Treasurer

Subcommittee Members Not Represented or in Attendance:

None

Others in Attendance:

Ms. Laura Gerard, Deputy Attorney General, Department of Justice
Mr. Steve McVay, Director of Investments and Cash Management, Office of the State Treasurer
Ms. Susan Steward, Policy Advisor, Office of the State Treasurer
Mr. John Krimmel, NEPC
Mr. Kevin Leonard, NEPC
Mr. Ian Spencer, NEPC
Mr. Phillip Nelson, NEPC

CALLED TO ORDER

Mr. Marvin called the meeting to order at 10:13 AM and introductions were made around the table.

APPROVAL OF THE MINUTES

A MOTION was made by Mr. Karia and seconded by Mr. Cook to approve the minutes from the meeting of the Cash Management Policy Board (Board), Investment Subcommittee (Subcommittee) on July 27, 2016.

MOTION ADOPTED UNANIMOUSLY

UPDATE ON INVESTMENTS GUIDELINES

Mr. McVay updated the Subcommittee on the current status of the revised guidelines posted on October 1, 2016 for public comment. To date, no public comment was received. Ms. Gerard informed the Subcommittee of the procedure moving forward and indicated that any technical changes would need a

OF THE CASH MANAGEMENT POLICY BOARD NOVEMBER 4, 2016

A Meeting of the Investment Subcommittee of the Cash Management Policy Board was held on November 4, 2016 at 10:00 AM in the Conference Room of the Office of the State Treasurer (OST)
Located at 820 Silver Lake Blvd., Suite 100, Dover, Delaware.

Subcommittee Members Represented or in Attendance:

Mr. John Flynn, Chair, Cash Management Policy Board
Mr. Dave Marvin, Chair, Investment Subcommittee
Mr. Mike Karia, Co-Chair, Investment Subcommittee
The Honorable Thomas J. Cook, Secretary, Department of Finance
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Mr. McVay informed the Subcommittee that Liquidity and Reserve Managers suggested technical changes during their meetings in October with OST. Ms. Gerard clarified for the Subcommittee that if the Chair determines the changes were substantive, then the procedure outlined previously would need to be followed with the guidelines reposted for public comment in December.

Memo from NEPC on Liquidity and Reserve Manager Suggested Changes

Mr. Krimmel presented a memo summarizing the proposed changes to the guidelines from the Liquidity and Reserve Managers. Proposed changes included increasing the maturity on fixed rate securities from date of settlement, eliminating the country-by-country list for permissible foreign investment, verification of credit quality from at least two of the three major credit agencies, and a US Treasuries minimum threshold.

Mr. Marvin recommended that the guidelines continue without change until a thorough review is completed. Mr. Krimmel stated he would keep these in mind until the liquidity analysis is complete.

The Subcommittee agreed to continue with the guidelines as they are presently written until the liquidity analysis is complete.

UPDATE ON THE LIQUIDITY ANALYSIS REPORT

NEPC Slide Presentation on Analysis

Mr. Krimmel introduced Mr. Spencer and Mr. Nelson from NEPC. Mr. Spencer reviewed NEPC's findings based on the historical data from OST of the cash management architecture. Mr. Spencer explained the methodology for itemizing the funds into three categories and reviewing the balances on a rolling monthly time frame. Mr. Spencer informed the Subcommittee that NEPC has accounted for the seasonality of cash flows in the analysis. Three scenarios were outlined that will be included in the final analysis for the Board.

Mr. Marvin asked if it was possible to have the study go back to fiscal years 2008 and 2009 to gauge the size of the draws during that period. Mr. Spencer noted this could be completed, depending on the availability of the data. Mr. McVay stated the data does exist and can be made available. Mr. Spencer stated this would be a valuable addition to the conceptual framework, especially in the development of a stress test environment.

UPDATE ON WELLS FARGO

Mr. McVay informed the Subcommittee that OST is monitoring Wells Fargo, both at the banking and investments level. Mr. McVay briefed the Subcommittee on the Banking Subcommittee's discussion earlier in the week surrounding Wells Fargo as the Direct Deposit services vendor for banking. Furthermore, the Banking Subcommittee agreed to bring the matter of the award of the Direct Deposit contract before the Board at the next meeting.

Mr. Marvin expressed his confidence that due to the amount of experience conveyed through their Board of Directors, that the legal situation surrounding Wells Fargo would not worsen. In reference to the Direct Deposit contract, Mr. Simpler explained that there are two other finalists who can perform the same services as Wells Fargo. Furthermore, Mr. Simpler reminded the Subcommittee that while OST was in negotiations with Wells Fargo, the current contract expired on June 30, 2016. At this time, the contract for direct deposit has not been consummated and will require a review by the Board to determine how to proceed.

Mr. Simpler stated that the Wells Fargo's investment management contract was still active. Marvin proposed taking no action for renewal of Wells Fargo's contract at this time for investment management.

Mr. Simpler and Mr. Marvin concurred that the Subcommittee could revisit the renewal at the February meeting.

The Subcommittee agreed to wait until the February meeting to readdress the renewal of Wells Fargo's investment management contract.

RENEWAL OF INVESTMENT MANAGER CONTRACTS

Mr. McVay updated the Subcommittee on the current status of the investment manager contracts. Mr. McVay recommended extensions for all managers, with the exception of Wells Fargo, for the period of one year.

A MOTION was made by Mr. Marvin and seconded by Mr. Karia to recommend the extension of the investment manager contracts, with exception of Wells Fargo, through May 2018.

MOTION ADOPTED UNANIMOUSLY

UPDATE ON CONVERSION TO NEW CUSTODIAN NORTHERN TRUST

Mr. McVay updated the Subcommittee on the status of the current custodian transition from Bank of New York Mellon to Northern Trust. The contract was finalized at the end of September, with Northern Trust to take possession of the assets on December 1, 2016.

OPERATING ACCOUNT STATUS

Mr. McVay distributed a table listing the most recent operating accounts and their status as of September 30, 2016.

Health Fund Account

Mr. McVay reported that as of November 1, 2016, the Health Fund has been closed and the assets transferred to the Schroders Reserve Account. Any interest to be paid out on this fund will be done as a blended rate of liquidity interest similar to the school and special fund payments.

Budget Reserve Account ("Rainy Day Fund")

Mr. McVay reported that JP Morgan had completed a series of tests on the Budget Reserve Account's current 1.2 percent cushion. Mr. Krimmel noted that NEPC analyzed JP Morgan's analysis to determine a sufficient cushion for the Budget Reserve Account under a stressed environment. Mr. Krimmel noted NEPC analyzed four separate scenarios, and concluded that the cushion would need to be increased from \$2.5 million to \$5.0 million.

Mr. Marvin stated that the change should be made and Mr. Simpler concurred. Mr. Simpler noted that the change in the cushion was operational, not a guideline change. The Subcommittee agreed that OST should move forward with the change.

Land and Water Endowment Cash Account

Mr. McVay discussed the Land and Water Cash Account previously invested in the BlackRock Fund. Mr. McVay reported that the BlackRock Fund transitioned to the floating rate net asset value (NAV) as

a result of the October Securities and Exchange Commission mutual fund rule changes.¹ Given this circumstance, the money market fund be changed to Federated Government Obligations fund. The change from BlackRock NEPC recommended to Federated will retain the fixed dollar NAV.

Outside Bank (Investment) Accounts

Mr. McVay updated the Subcommittee on the status of the outside bank accounts related to investments. He reminded the Subcommittee that outside bank accounts included accounts opened up by schools and other agencies for various reasons under the State's EIN. Previously, OST noted at least four investments accounts were opened by organizations using the State's EIN. Based on the most recent Generally Accepted Accounting Principles report submitted to the Department of Accounting, approximately \$5.6 million dollars were held in these accounts. Three accounts opened by school districts for scholarships funds held approximately \$700,000, and one account for the Court of Chancery held nearly \$4.9 million.

Mr. Simpler remarked the \$4.9 million was not earmarked for any special projects and that the Court of Chancery had created their own guidelines managing the funds at PFM. Mr. Simpler stated that there needed to be more investigation of these funds and he proposed three suggestions on how we could handle the situation: (I) we could have the Court of Chancery adopt our guidelines for the funds, (II) the Board could adopt their guidelines strictly for the \$4.9 million, (III) the board might be able to delegate the courts discretion to manage their own funds.

Mr. Marvin expressed no great interest in taking on responsibility for the funds due to the lack of information around the situation. Mr. Simpler suggested we move the money back under OST's purview and keep it separate for the Court of Chancery. However, they would be able to continue with their investment management services at PFM and adhere to the Board's guidelines. Mr. Flynn and Mr. Marvin agreed with this approach.

PUBLIC COMMENTS

No members of the public present for comment.

NEXT MEETING

Mr. Marvin announced that the next meeting is scheduled to be telephonic in February 2017.

ADJOURNMENT

A MOTION was made by Mr. Marvin and seconded by Mr. Karia to adjourn the meeting of the Investment Subcommittee of the Cash Management Policy Board at 12:05 PM

MOTION ADOPTED UNANIMOUSLY

¹ Prior to October 2016, the BlackRock Fund and several money funds kept their net asset value fixed at one dollar. However, the Securities and Exchange Commission in October 2016 modified the rules relating to money funds and fees associated with non-governmental funds requiring these funds to switching to a floating net asset value.

Respectfully submitted,

David Marvin
Chair for the Investment Subcommittee

Mike Karia
Co-Chair for the Investment Subcommittee